Additional Views to Accompany
H.R. 49, the "Internet Tax Nondiscrimination Act"

We offer these additional views to emphasize our continued commitment to the vitally important issue of State sales tax simplification which, in past terms of Congress, has been linked to the moratorium on Internet access taxes. Because the moratorium and simplification issues have been decoupled, we support H.R. 49, as amended.[1] However, our commitment to the State sales tax simplification project derives from the ongoing need to develop a "level playing field" for the collection of sales taxes by all forms of retailers. We believe that we must address this issue expeditiously and with similar vigor.

As a result of the 1992 Supreme Court decision in *Quill v. Heitcamp,*[2] there exists a disparity in the tax treatment of similarly situated sellers. *Quill* held that absent congressional authorization, States are not permitted to require sellers to collect taxes unless, among other things, the seller has a "substantial nexus" with the State. Congress recognized the potential impact of the *Quill* decision on Internet transactions when the ITFA was passed. Indeed, ITFA called for the creation of a commission – the Advisory Commission on Electronic Commerce (ACEC)[3] – to conduct a study of the impact of electronic commerce on all forms of taxation, and specifically the issues concerning the state and local taxation of transactions over the Internet. In April 2000, the ACEC delivered its final report to Congress.[4] Although the ACEC was unable to obtain the requisite consensus (two-thirds vote) required by ITFA on the issue of Internet sales tax, the report included a majority policy recommendation that states simplify their sales and use tax systems. Officially established in March 2000, the Streamlined Sales Tax Project (SSTP) is a collection of thirty-nine States and the District of Columbia organized to accomplish that goal.[5]

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[1] Mr. Watt offered an amendment during the markup of H.R. 49 in the Subcommittee on Commercial and Administrative Law in May 2003. The amendment equalizes the treatment of all providers of Internet access regardless of technology. At Full Committee markup, Mr. Cannon, Chairman of the subcommittee, joined Mr. Watt in offering the amendment which passed with strong bipartisan support. (Ms. Jackson-Lee also offered two amendments. One, designed to preserve the grandfathered States' authority to collect Internet access taxes, and the other, to establish a system to phase out those States' collection of access taxes were both defeated by voice vote.)

[2] 504 U.S. 298 (1992). *Quill* held that in order to sustain an interstate sales tax, the tax must apply to an activity with a substantial nexus with the taxing State; be fairly apportioned; not discriminate against interstate commerce; and be fairly related to the services provided by the State. In the event a good is sold across interstate lines without being subject to a sales tax, the purchaser remains subject to a comparable "use tax" within his or her own State.

[3] The ACEC consisted of nineteen members. Eight were representatives of State and local governments; eight were from business and consumer groups, and three were representative of the Federal government from the offices of the U.S. Trade Representative, the U.S. Secretary of Commerce, and the U.S. Secretary of the Treasury.

[4] ACEC offered consensus recommendations in only three areas unrelated to the sales tax issue: (1) the digital divide; (2) privacy implications of the Internet; and (3) international trade and tariffs.

[5] The participating States are: Alabama, Arizona, Arkansas, Florida, Illionois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maine, Maryland, Michigan, Minnesota, Mississippi, Missouri, Nebraska, Nevada, New Jersey, North Carolina, North Dakota, Ohio, Oklahoma, Pennsylvania, Rhode Island, South Carolina, South

Since that time the SSTP has made substantial progress towards establishing a uniform, modernized and streamlined system of sales and tax collection and administration. Presently, over thirty States, collectively referred to as the Streamlined Sales Tax Implementing States (SSTIS), have adopted an interstate tax agreement.[6]

The Majority has indicated that hearings will be held to address the streamlining issue this fall. We welcome this opportunity because failure to revisit this issue raises many of the identical concerns we expressed in rejecting long term extension of the moratorium last Congress. Those concerns, however, are magnified exponentially in light of the tremendous budget shortfalls and deficits that many States are currently experiencing. Moreover, the significant security burdens imposed upon the States post 9/11 suggest that these burdens will persist.[7]

All interested parties–retailers (both electronic and traditional), State and local governments, and consumers–will suffer if we continue to avoid addressing this issue. The problems with the present system from the perspective of the retail industry are multifaceted. First, the complexity of the tax system is daunting. There are presently over 6,500 taxing jurisdictions in the United States when all State, county and municipal authorities are included. The jurisdictions generally require separate collection, have overlapping definitions of goods and services subject to tax, specify differing sets of exemptions and *de minimus* thresholds, have differing bad debt rules, and varying sets of forms and audit systems. Any retailer with a physical nexus to a State is subject to a myriad of confusing and complex State and local taxes. This carries with it large paperwork and collection burdens. Second, the legal uncertainty of the present system can be harmful, even for remote sellers, because of the many questions left unresolved by the *Quill* decision and under ITFA. Determining what constitutes a "substantial nexus" for a particular retailer can be highly subjective. Third, the current disparate tax treatment between traditional "brick and mortar" retailers and remote sellers has the potential to cause continuing economic distortion.[8] Yet the present system, by creating a tax incentive to be located

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Dakota, Tennessee, Texas, Utah, Vermont, Virginia, Washington, West Virginia, Wisconsin, and Wyoming.

[6] Under the procedures of the STTP, the agreement must now be converted into legislation by the participating States.

[7] The States are currently facing an aggregate revenue shortfall of $21.5 billion (23% greater than the Nov. 2002 projections), and that number is projected to grow to $53.5 billion for FY 2004. Moreover, according to statistics compiled by U.S. Conference of Mayors, a Tom Ridge-imposed Code Orange terror alert is projected to cost State government $70 million per week.

[8] In an industry such as retail sales, where a 1-2% profit margin may be standard, a 6-8% sales tax differential can offer a significant price advantage.

in a remote physical location, threatens to do exactly that.[9] This, in turn, has the potential to harm local employment and real estate values.

The impact on State and local governments of a prolonged maintenance of the current system carries with it the potential for significant financial loss at a time when States are suffering devastating budget crises. Sales taxes constitute the most important State and local revenue source, far greater than income and property taxes, with the Census Bureau estimating that 47.9% of State and local revenues come from sales taxes. Projections of annual online sales were estimated to exceed $100-300 billion in 2002. That translates into a loss for State and local governments of as much as $20 billion in uncollected sales taxes under the present system.[10] Loss of sales tax revenues could have a grave impact on critical services such as police, safety, health and education.

Finally, the present system could significantly harm individual consumers. The loss of sales taxes from remote sales may lead to increasing income and property taxes or declining public services. A separate concern is the adverse impact of the present bifurcated system on the poor and minorities. According to a study by the U.S. Department of Commerce, wealthy individuals were 20 times more likely to have Internet access, while Hispanics and African Americans were far less likely to have such access.[11] As a result, poor and minority consumers are more likely to buy locally (often with cash) and thus, face a greater sales tax burden than those with credit and broader access to the Internet.

Since passage of the ITFA in 1998, State governments, business leaders and consumer advocates have coalesced to address the thorny issue of interstate taxation and e-commerce. Reportedly, significant progress has been made in reforming and simplifying State laws. The Judiciary Committee has taken an important step in passing H.R. 49, as amended, to provide a level playing field for all providers of Internet access. The Committee should also be on the forefront of providing the States with the necessary authority to collect sales taxes in a uniform and non-discriminatory manner from all remote sellers, including those conducting business over the Internet. Hearings devoted to the State tax simplification issue will enable us to consider whether we should approve an interstate process that addresses the simplification issue.

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[9] Perversely, the present system also creates an incentive, in terms of State sales taxes, to be located *outside* of the United States.

[10] *See* Donald Bruce and William F. Fox, *E-Commerce in Context of Declining State Sales Tax Basis,* Center for Business and Economic Research (CBER), University of Tennessee, Knoxville, February 2000.

[11] *Falling Through the Net II: New Data on the Digital Divide, National Telecommunications and Information Administration,* National Telecommunications and Information Administration, July 1998 (httpL//www.ntia.doc.gov/ntiahome/net2/falling.html).

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